No. 229

In the Supreme Court of the United States

OCTOBER TERM, 1939

THE REAL ESTATE-LAND TITLE AND TRUST COMPANY, PETITIONER

v.

THE UNITED STATES OF AMERICA

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE UNITED STATES

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OPINIONS BELOW

The opinion of the trial court (R. 287–292) is not reported. The opinion of the Circuit Court of Appeals (R. 319–326) is reported in 102 F. (2d) 582.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on March 13, 1939. (R. 327.) A petition for rehearing was denied May 1, 1939. (R. 328.) The petition for a writ of certiorari was filed July 26, 1939, and was granted October 9, 1939. (R. 329.) The jurisdiction of this Court rests on Section 240 (a) of

the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

Taxpayer, upon its incorporation, became the owner of two duplicate title abstract plants designed and used for the same general purpose. Immediately upon acquisition and prior to the commencement of the taxable year one was stored, without thereafter being kept up-to-date.

1. Does the lack of utility to taxpayer of the stored plant result from obsolescence that is deductible from gross income, or is it merely attributable to deliberate duplication of facilities for which no deduction is allowable?

2. If taxpayer is not entitled to an obsolescence deduction, is it entitled to a loss deduction on account of the lack of utility to it of the stored plant?

STATUTE AND REGULATIONS INVOLVED

The statute and regulations involved will be found in the Appendix, *infra*, pp. 48–51.

STATEMENT

This suit was instituted by the taxpayer to recover income taxes paid with respect to its fiscal year ending October 31, 1928.

The taxpayer is the product of a merger of three corporations which was consummated on October 31, 1927, pursuant to an agreement of October 3, 1927. (R. 20–22.) Two of the constituent corporations, the Real Estate Title Insurance and Trust Company and

the Land Title and Trust Company, had been engaged in the title insurance business, and together owned two of the three principal title abstract plants in Philadelphia. (R. 35.) For purposes of the merger the two plants were valued at $800,000 each, although immediately prior thereto the Land Title plant had been carried at $275,000 and the Real Estate Title plant at $143,000. (R. 22.) Before and at the time of the merger the parties thereto knew that the new corporation was about to acquire two title plants designed and used for the same general purpose. (R. 22–23.) Only one such plant could be used advantageously by any one company. (R. 29, 118–119, 123.)

Both were excellent plants, and the same results could be obtained from each. Together they constituted the two most complete plants in the city. (R. 80.) A committee designated in October, 1927, by the combining companies to determine which of the two plants would be used by the new corporation recommended prior to the merger that the Real Estate Title plant be tried in view of greater economy in operation. (R. 31–32, 50–51.) Accordingly, the records comprising the Land Title plant were stored in a basement, and by the latter part of October, 1927, the daily additions required to keep the plant up-to-date were discontinued. (R. 32–33.) Thereafter, the only use made of those records was to ascertain what insurances were involved in connection with the forthcoming November sheriff's sales, and "from time to time, there has been, very occasionally, a check-up of some information from material in the plant to save a visit to City Hall". (R. 57.)

During 1928, the taxpayer set a price upon the stored plant to a prospective purchaser of $1,000,000. (R. 33–34, 41, 297.) The good will of that plant was said to be "very substantial". (R. 96–97.) There was no testimony as to any improvements in the art of title insurance or as to any new or improved methods the lack of which would result in obsolescence of a plant not having those advantages.

In its report to the Pennsylvania Department of Revenue for the two-month period ended December 31, 1927, and for the calendar years 1928, 1929, and 1930, taxpayer listed among its assets an item designated as "Title Plant," valuing it first at $1,600,000, but showing a reduction of $50,000 therefrom for each succeeding year. The reports for the years 1931 and 1932 specifically indicated that the item "Title Plant" referred to both plants, and stated that since they were duplicates "one of them was of no further use" and was being amortized. (R. 27–29.)

Ownership of a complete land title abstract plant is an invaluable aid in obtaining title insurance business (R. 36), and is a source of great prestige (R. 119). Certain important customers, such as large mortgage and insurance companies, would not give their title insurance business to a company which did not own such a plant. (R. 36, 119.) Taxpayer never advertised the Land Title plant for sale (R. 34), although two companies might have been interested in its purchase (R. 119). There is no evidence that taxpayer ever offered to sell the plant for less than $1,000,000, although it is financially impossible for one company to operate two

plants. (R. 123.) The suppression of one of the three existing abstract plants was a financial benefit to the other companies owning such plants, since the elimination of competition among the so-called plant companies was highly advantageous. (R. 119–120.)

The District Court ruled that taxpayer was entitled to a deduction on account of obsolescence for its fiscal year ended October 31, 1928, in the amount of $875,000. (R. 292.) The Circuit Court of Appeals reversed, holding that no deduction for obsolescence was allowable.

SUMMARY OF ARGUMENT

The inutility to taxpayer of the Land Title plant arises from deliberate duplication of assets, which, as a matter of law, is not an occasion for an obsolescence allowance. It is not comprehended within any established definition of obsolescence, nor is the purpose of the statute such as to include it. Since it was known at the time of the merger that taxpayer would acquire duplicate plants, there was no intention to use one of them at time of acquisition. Accordingly, whatever loss petitioner may have suffered was attributable, not to obsolescence, but to deliberate duplication of facilities.

Moreover, the necessary period of obsolescence, of a duration greater than the taxable year, has not been established by taxpayer. Even if the circumstances were such as to satisfy the legal prerequisites for an obsolescence deduction, taxpayer's claim must be denied because the Land Title plant did not in fact become obsolete during the taxable year.

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The court below indicated that it did not believe that taxpayer had satisfied the statutory requirement of *use* in the trade or business, but did not rest its decision upon that ground. The Circuit Court of Appeals would have been entirely justified in denying the obsolescence deduction for failure to satisfy that statutory requirement, for there is no adequate evidence to support the finding that the Land Title plant was "used" in the trade or business of taxpayer.

Taxpayer's contention that it is entitled to a deduction on the theory of abandonment, under the loss provision of the statute, Section 23 (f), is ill founded. First, taxpayer may not now raise the question of an abandonment deduction because its claim for refund was predicated exclusively on obsolescence, under Section 23 (k), and only the question of an obsolescence allowance was presented to, or considered by, the District Court. Furthermore, even if the issue is properly before the Court, it is without substance. The plant in question was never abandoned; it had substantial value and was simply stored.

Moreover, the record persuasively shows that the purpose motivating the acquisition of the Land Title plant was the desire to eliminate competition. Therefore, the obsolescence deduction and the loss deduction on grounds of abandonment should both be denied for that reason as well.

If it be held, notwithstanding the foregoing considerations, that taxpayer is entitled to some deduction, we then urge that the amount allowed by the District Court is grossly excessive. The court erred in not reducing the allowance by the value of that portion of the plant

which was not allegedly obsolete or abandoned. Moreover, the basis founded upon the March 1, 1913 value found by the District Court is excessive and not supported by the evidence. There was also error in the failure to exclude the value of the plant's good will in calculating the deduction, since good will is not a proper subject for an obsolescence allowance.

ARGUMENT

I

THE COURT BELOW CORRECTLY HELD THAT TAXPAYER IS NOT ENTITLED TO ANY DEDUCTION UNDER THE PROVISIONS OF SECTION 23 (k) OF THE REVENUE ACT OF 1928

In denying the claimed deduction on account of the alleged obsolescence of the Land Title plant, the court below based its decision upon two distinct grounds. Taxpayer is not entitled to a deduction under Section 23 (k) because (1) as a matter of law, duplication of assets is not a proper occasion for an obsolescence allowance; and (2) the Land Title plant did not in fact become obsolete during the taxable year. We contend that the Circuit Court of Appeals was correct in both respects, and that either ground is adequate to sustain the result below.

A. AS A MATTER OF LAW, DUPLICATION OF ASSETS IS NOT A PROPER OCCASION FOR AN OBSOLESCENCE ALLOWANCE

1. The term "obsolescence", as used in the Revenue Act, has been defined generally as the "condition or process by which units gradually cease to be useful or profitable as a part of the property, on account of changed conditions." See *Burnet* v. *Niagara Brewing*

Co., 282 U. S. 648, 654.[1] This Court, while refraining from formulating any comprehensive definition, has stated that "Obsolescence may arise from changes in the art, shifting of business centers, loss of trade, inadequacy, supersession, prohibitory laws and other things which, apart from physical deterioration, operate to cause plant elements or the plant as a whole to suffer diminution in value." *United States Cartridge Co.* v. *United States*, 284 U. S. 511, 516; *Burnet* v. *Niagara Brewing Co.*, 282 U. S. 648; *Gambrinus Brewery Co.* v. *Anderson*, 282 U. S. 638.[2]

[1] The Bureau of Internal Revenue has defined obsolescence "as the process of becoming obsolete, brought about by the progress of the arts and sciences, changed economic conditions, legislation, or otherwise, whereby it can be predicted with reasonable accuracy that property used in the trade or business will be useless at a definite future date prior to the expiration of the normal useful life of the property." Bureau Bulletin "F" (January, 1931) 2. See also Article 206, Regulations 74, Appendix, *infra*. p. 51.

[2] It may be noted, at this point, that there are two generally recognized and more or less distinct types of obsolescence. The first, frequently designating "extraordinary obsolescence", involves a relatively sudden diminution of useful value consequent upon some radical change, while the second contemplates a gradual exhaustion of the utility of a particular property due to the accumulated effect of small improvements or changes introduced from time to time in the art or industry generally which render the property relatively less efficient, and which experience shows are practically certain to occur. Obsolescence of the second type can usually be anticipated with the same degree of accuracy as ordinary depreciation through physical exhaustion and wear and tear, and is frequently referred to as "normal obsolescence". No separate cognizance is taken of such normal obsolescence, its existence being recognized, if at all, in the fixing of the annual depreciation rate. See 2 Paul and Mertens, *Law of Federal Income Taxation*, Section 20.41; Montgomery, *Federal Income Tax*

In asserting that taxpayer is not entitled to the deduction for obsolescence allowed by Section 23 (k) of the Revenue Act of 1928, we do not contend, as taxpayer implies (Br. 17), that a title abstract plant may not, when the requisite facts have been shown, be a proper subject for an obsolescence deduction. Our position is predicated upon the taxpayer's total failure to demonstrate and upon the absence of any finding that the inutility to it of the Land Title plant was attributable to any circumstance comprehended within the established definitions of obsolescence or within this Court's enumeration of the types of occurrences giving rise to it, as set out above. Aside from the merger creating the taxpayer corporation, as a result of which taxpayer came into possession of two duplicate plants, and taxpayer's consequent voluntary discontinuance of current entries in the Land Title plant, the record is totally devoid of even the suggestion that there occurred any change in the conditions affecting the business of title insurance in Philadelphia tending to decrease the utility of the Land Title plant during the taxable year. No loss of trade, shifting of business centers, or substantial diminution in the need for the services of title insurance companies has been shown. Moreover, there is no testimony in the record to the effect that the Land Title plant was rendered obsolete by the development of new or improved techniques for the collection, re-

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Handbook (1936–1937) 674–675; Bureau of Internal Revenue Bulletin "F", January, 1931. But even in the case of "extraordinary" obsolescence there must be a period in excess of one year; otherwise, the deduction must be sought under the loss provisions of the statute rather than as an allowance for obsolescence. See pp. 16–22, *infra*.

cording, or utilization of information pertaining to real estate titles.[9] Neither was there a showing of prohibitory or restrictive legislation, supersession, or other factor having deleterious effect upon the usefulness of the Land Title plant. Both of taxpayer's plants were designed and used for the same general purpose. (R. 22–23.) Presumably, therefore, if the alleged obsolescence were the result of any of the foregoing factors, both plants would have been equally affected, yet no claim for an obsolescence deduction was made on account of taxpayer's other plant. The court below was thus correct in stating that such impairment of the utility of the Land Title plant as occurred during the taxable year was caused solely by voluntary duplication and taxpayer's consequent decision to store the plant and refrain from making the daily entries necessary to keep it up to date.

We submit that voluntary duplication of assets, as a matter of law, is not an occasion for an obsolescence deduction, and that the court below rightly so held. Voluntary duplication is not comprehended within any established definition of obsolescence, or this Court's enumeration of the types of situations which may constitute occasions for an obsolescence allowance. Moreover, as pointed out by the Circuit Court of Appeals, this Court's statements as to the circumstances giving rise to obsolescence and the accepted definitions of the term both indicate that the purpose of the statute in

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[9] There was evidence that some plants had adopted photostating devices, but it was not shown that the absence of such equipment rendered a plant obsolete, and indeed the taxpayer herein did not employ such equipment in either of its plants (R. 87).

granting the allowance is to permit a taxpayer to regain capital invested by him in machinery, equipment or other property when such machinery, equipment or other property becomes less useful because time itself brings improvements or changed conditions. See *Columbia Malting Co.* v. *Commissioner*, 1 B. T. A. 999, 1001; *Corsicana Gas & Electric Co.* v. *Commissioner*, 6 B. T. A. 565, 568–569. As concisely stated by the court below, "obsolescence may be claimed when machinery or a plant suffers loss in use not because of action or lack of it upon the part of the taxpayer, but because of the effect of general conditions over which he has no control." (R. 324.)

We are aware of no authority holding that a deduction for obsolescence is allowable where the uselessness of an asset arises solely from unnecessary and deliberate duplication and a consequent voluntary failure to maintain the duplicated asset in perfect operating order. Taxpayer cites and places principal reliance (Br. 15–17) upon the decision of the Circuit Court of Appeals for the Eighth Circuit in *Crooks* v. *Kansas City Title & Trust Co.*, 46 F. (2d) 928, but that case did not so hold, nor is it in conflict with the decision below.

In urging that the decision of the court below be affirmed, we do not argue that the *Crooks* case was incorrectly decided on the basis of the facts therein. Still less do we assert that a title abstract plant may never be the subject of a proper obsolescence deduction. The court below did not so hold, and we make no such claim. We contend only that the *Crooks* case does not support taxpayer's position that a deduction for obsolescence

may be occasioned by voluntary duplication, and that it is readily distinguishable in several crucial particulars from the case at bar.

In the *Crooks* case, the court allowed a deduction for obsolescence of certain abstract plants. It found that taxpayer purchased them "for the purpose of using them in its business" (p. 928). The court also found that it was thought (p. 929) that they "could be used to advantage in the abstract and title guaranty work of the taxpayer", and at least part of the records they contained were so used. The deduction was allowed, not on grounds of duplication, but because taxpayer established that the plants would become obsolete over the period 1921–1930 as a result of "new and modern methods" which "tended to supplant the methods employed" (p. 929). Since taxpayer there made no claim for obsolescence until the plants had been in its possession for six years, it is clear that duplication was not the basis of its claim. Rather, the plants in question were found upon trial to be inefficient, and new entries were discontinued for that reason. Thus, it is apparent that the *Crooks* case is authority only for this proposition: where an asset is bought for the purpose of use in the business, and is in fact so used, and subsequently is shown to be in process of becoming obsolete by reason of the development of improved methods, the cost of such asset may be deducted, *pro rata,* over the period of obsolesence established. Manifestly, the case cannot possibly be construed to hold that where taxpayer obtains an asset which, at the time of acquisition, is useless to him because it is a duplicate of one he already owns,

he may, in the year of acquisition, take an obsolescence deduction in the full amount of the value of the duplicate asset.

As is apparent from the foregoing, the *Crooks* case is readily distinguishable from the instant case in several significant particulars: (1) The taxpayer in the *Crooks* case purchased the abstract plants for the purpose of using them in its abstract and title guaranty business and in the belief that they could be used to advantage in such business. In the case at bar, on the other hand, the taxpayer knew, when it acquired the Land Title and Real Estate plants, that one of them was an unnecessary duplicate, useless in its business. This was admitted in taxpayer's report to the Pensylvania Department of Revenue (R. 29). And the testimony of taxpayer's title officer indicates clearly that it was known when the Land Title plant was acquired that it would not be useful in taxpayer's business. (R. 50.) Finally, there is the undisputed fact that the Land Title plant was stored in the basement during late October and early November, 1927, immediately upon the organization of the taxpayer corporation. (R. 57, 296.) (2) There was absolutely no showing, in the instant case, of any new or improved techniques that would render either plant obsolete, while in the *Crooks* case the court stated (p. 929) that "new and modern methods" had "tended to supplant the methods employed". (3) In the *Crooks* case new daily entries were discontinued because the plants were found upon trial to be inefficient, whereas the present taxpayer discontinued the daily entries only because

the Land Title plant was a superfluous duplicate. (4) Taxpayer in the *Crooks* case established a period of obsolescence from 1921 to 1930, and claimed the deduction *pro rata* over those years, while the instant taxpayer did not, although required to do so by Article 206 of Regulations 74. (5) No claim for obsolescence deduction was made in the *Crooks* case until the plants had been in taxpayer's possession for six years. The present taxpayer claimed a deduction for total obsolescence immediately.

We have found only one case in which an obsolescence deduction was claimed on account of property which taxpayer had no intention of using at the time of acquisition. In *Columbus Brick & Tile Co.* v. *Commissioner*, 26 B. T. A. 794, taxpayer purchased a brick and clay plant, which included certain burning and drying equipment in process of being dismantled because of obsolescence at the time of purchase. Taxpayer's claim for an obsolescence deduction on that equipment was denied because it knew, at the time of purchase, that the equipment would not be used.

Likewise, it has been held that a bad debt deduction is not allowable where the debt was worthless when acquired by the taxpayer. *Eckert* v. *Burnet*, 283 U. S. 140, 141; *Dexter* v. *Commissioner*, 99 F. (2d) 769, 773 (C. C. A. 1st); *Kinkead* v. *Commissioner*, 71 F. (2d) 522, 523 (C. C. A. 3d); *In re Park's Estate*, 58 F. (2d) 965, 967 (C. C. A. 2d), certiorari denied, 287 U. S. 645. Cf. *Voliva* v. *Commissioner*, 36 F. (2d) 212, 213 (C. C. A. 7th). And many analogous cases establish the general rule that no loss deduction is allowable where tax-

payer knowingly acquires property of no utility to it. Thus, where land upon which there is a building is purchased with the intention of demolishing, rather than using the building, no loss deduction may be taken for the value of the building. *Providence Journal Co.* v. *Broderick,* 104 F. (2d) 614 (C. C. A. 1st); *Liberty Baking Co.* v. *Heiner,* 37 F. (2d) 703 (C. C. A. 3d); see *Union Bed & Spring Co.* v. *Commissioner,* 39 F. (2d) 383, 385 (C. C. A. 7th); cf. *Anahma Realty Corporation* v. *Commissioner,* 42 F. (2d) 128 (C. C. A. 2d), certiorari denied, 282 U. S. 854; *Young* v. *Commissioner,* 59 F. (2d) 691 (C. C. A. 9th), certiorari denied, 287 U. S. 652; *Spinks Realty Co.* v. *Burnet,* 62 F. (2d) 860 (App. D. C.), certiorari denied, 290 U. S. 636. Likewise, a taxpayer has been held not entitled to a loss deduction where he purchases and scraps a competitor's plant in order to eliminate competition. *Newspaper Printing Co.* v. *Commissioner,* 56 F. (2d) 125 (C. C. A. 3d).[4] Nor is taxpayer entitled to a loss deduction when he buys machinery for which, it develops, he has no use. *Flexible File Co.* v. *Commissioner,* 13 B. T. A. 909, affirmed, *per curiam,* 41 F. (2d) 997 (C. C. A. 6th). Similarly, the Treasury Department has ruled that the expenditure for land title abstract books "may not be deducted as a loss by reason of the purchaser's claim that they are of no service to it because it already owns

[4] The court below indicated, by its reference to the *Newspaper Printing Co.* case, that it believed the Land Title plant was acquired for the purpose of eliminating competition and that the deduction claimed might be disallowed for that reason. (R. 326.) This point is discussed *infra*, pp. 38–41.

another set of the same records." O. D. 1049, 5 Cum. Bull. 175 (1921).

By parity of reasoning, the taxpayer's claim for an obsolescence deduction should be denied since it voluntarily acquired duplicate plants, one of which it did not intend to use.

2. Moreover, taxpayer is not entitled to the deduction for obsolescence because it has failed to establish a period of obsolescence of a duration greater than one year at the end of which the property would be obsolete. As stated in *Tennessee Fibre Co.* v. *Commissioner,* 15 B. T. A. 133, 140, the statutory provision for obsolescence "is intended to care for losses of capital which take place *over a longer period than the taxable year.*" [Italics supplied.] And this Court has plainly indicated that the allowance for obsolescence, like the deduction on account of depreciation, is an *annual* allowance (*Gambrinus Brewery Co.* v. *Anderson*, 282 U. S. 638, 645):

> The statute contemplates annual allowance for obsolescence just as it does for exhaustion, wear and tear. That is necessary in order to determine true gain or loss because postponement of deductions to cover obsolescence until the property involved became obsolete would distort annual income. It is well understood that exhaustion, wear, tear or obsolescence cannot be accurately measured as it progresses and undoubtedly it was for that reason that the statute authorized "reasonable" allowances to cover them in order equably to spread that element of operating expenses through the years. * * *

Accordingly, when an asset becomes worthless during the taxable year only, no deduction for obsolescence is allowable. *Zakon* v. *Commissioner*, 7 B. T. A. 687.

In *Olean Times-Herald Corporation* v. *Commissioner*, 37 B. T. A. 922, two newspapers, the Olean Times and the Olean Herald, each having its own printing plant, combined in 1932, and thereafter used the plant of the Times to the exclusion of the other. In the returns of the combined corporation for 1933 and 1934, obsolescence deductions were claimed. The Board said (at pp. 924-925):

> "Obsolescence as used in the statute is the state or process of becoming obsolete, and the provision allowing a deduction therefor is intended to care for losses of capital which take place over a longer period than the taxable year." *Tennessee Fibre Co.,* 15 B. T. A. 133; *William Zakon,* 7 B. T. A. 687. Thus, it is necessary for one claiming such a deduction to establish a period longer than the taxable year over which period the asset is becoming obsolete and at the end of which period it will be obsolete. * * *

It will be noted that the rule that obsolescence must be established over a period longer than the taxable year at the end of which the asset will be obsolete scrupulously follows the requirement of the regulations to the effect that obsolescence is allowable only when the taxpayer clearly shows that his property is being affected by economic conditions "that *will* result in its being abandoned *at a future date*". (Italics supplied.) Treasury Regulations 74, Article 206. See

I. T. 1775, II-2 Cum. Bull. 145 (1923); O. D. 381, 2 Cum. Bull. 138 (1920); Bureau of Internal Revenue Bulletin "F", January, 1931. Similarly, it gives effect to the definition of obsolescence as a "*process* by which units *gradually* cease to be useful * * * on account of changed conditions". (Italics supplied.) See *Burnet* v. *Niagara Brewing Co.*, 282 U. S. 648, 654. It also preserves the distinction between obsolescence and loss of useful value contemplated by Regulations 74 in Article 206 and Article 173. Article 173, relating to "loss of useful value", requires proof of some change in conditions whereby the usefulness of an asset is "suddenly terminated", and allows a loss deduction in the year in which such termination occurs. On the other hand, Article 206, dealing with obsolescence, requires a showing that the property will become useless at some future date, and contemplates deductions in the years prior to the year in which complete uselessness will result. *State Line & Sullivan R. Co.* v. *Phillips*, 98 F. (2d) 651 (C. C. A. 3d), certiorari denied, 305 U. S. 635.

Examination of the cases in which this Court has upheld a deduction under the obsolescence provision of the revenue act reveals that, with but one exception,[5] the taxpayer established the existence of a period of obsolescence of a duration greater than the taxable year, at

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[5] In *United States Cartridge Co.* v. *United States*, 284 U. S. 511, a deduction for obsolescence of certain buildings was allowed in 1918, because of the Armistice, although no period of obsolescence had been established. Where, as in the *U. S. Cartridge* case, a total loss of useful value occurs in one taxable year, it is believed the regulations contemplate that a loss deduction, not an obsolescence deduction, will be allowed. Regulations 74, Article 173. See

the end of which it was reasonable to believe that property would be completely obsolete. Thus, in *Gambrinus Brewing Co.* v. *Anderson*, 282 U. S. 638, this Court stated (at p. 640):

> January 31, 1918, it had become common knowledge and was known to plaintiff that prohibition would become effective and that as a result plaintiff and others engaged in that business would suffer obsolescence in the value of their capital assets. Prohibition did become effective January 16, 1920. * * * As a result of prohibition and beginning January 31, 1918, and ending January 16, 1920, plaintiff suffered obsolescence of such buildings equal to such depreciated cost which should be ratably apportioned over that period. * * *

In *Burnet* v. *Industrial Alcohol Co.*, 282 U. S. 646, where an obsolescence deduction was allowed on authority of the *Gambrinus* case, this Court observed that the Board of Tax Appeals found that the period of obsolescence over which the deduction could be taken was from December 18, 1917, to January 16, 1920. Likewise, in *Burnet* v. *Niagara Brewing Co.*, 282 U. S. 648, it was said (at p. 656):

discussion, *infra*, pp. 21–22. In any event this Court was not called upon to decide the question of whether, where useful value is suddenly and completely terminated, the proper deduction is to be taken under the loss provision of the statute, or under the obsolescence provision. The Government argued only that no obsolescence deduction should be allowed because, by Section 234 (a) (8) of the Revenue Act of 1918, amortization of war production facilities was authorized. This Court held only that the amortization provision did not exclude an obsolescence allowance.

> The facts found clearly show that obsolescence commenced about the beginning of 1918 and that the property became obsolete upon the taking effect of prohibition in January, 1920. * * *

Similarly, in the case on which taxpayer places principal reliance, *Crooks* v. *Kansas City Title & Trust Co.*, 46 F. (2d) 928 (C. C. A. 8th), as pointed out by the court therein, the taxpayer complied exactly with the requirement of the Regulations and Treasury rulings by establishing that the four abstract plants on which the obsolescence deduction was claimed would become obsolete over the period 1921–1930, and would be useless by that latter date.

Taxpayer cites, and quotes at considerable length from the decision of the Circuit Court of Appeals for the Eighth Circuit in *United States* v. *Wagner Electric Mfg. Co.*, 61 F. (2d) 204. (Br. 19–21.) That case, it is argued, establishes that an obsolescence deduction need not be based on a process of obsolescence going on over any period of time, but may be allowed where an asset becomes obsolete "over night". (Br. 22.) However, that case merely held that, as a result of the Armistice, a *portion* of the value of machinery and equipment used in the manufacture of shells constituted a proper deduction in 1918 on account of obsolescence, and that the remainder should be deducted in 1919. Moreover, the court was not confronted with, and did not undertake to decide, the question of whether the proper deduction for the destruction of the utility of the shell manufacturing plant by the Armistice was a deduction for abandonment under the loss provision

of the statute or an obsolescence deduction. The Government argued only that the method used by the lower court in determining the amount of obsolescence attributable to the year 1918 was improper, and the court itself stated that (p. 205) "The only question presented is: How much, if any, of the admitted loss of $175,-866.49 should be attributed to the year 1918?" Accordingly, the *Wagner Electric* case may scarcely be regarded as an authority for the proposition that it is unnecessary, when claiming a deduction under the obsolescence provision of the revenue act, to establish a period of obsolescence extending over a time longer than the taxable year.

The contention here made that a deduction for obsolescence may not be granted unless it be shown that the process of obsolescence extends over a period greater than the taxable year does not require us to contend that in a case where the loss of useful value takes place due to obsolescence entirely within the taxable year the taxpayer is thereby denied the possibility of any deduction. In such a case, the taxpayer is entitled to a deduction, but the deduction should be claimed for the loss of useful value under the loss provisions of the statute, not under the obsolescence provision. O. D. 753, 3 Cum. Bull. 171 (1920); *Zakon* v. *Commisisoner,* 7 B. T. A. 687. See Regulations 74, Articles 173, 206. Thus, in 2 Paul and Mertens, *Law of Federal Income Taxation* (1934), § 20.111, it is said (p. 659):

> Extraordinary obsolescence where the usefulness of an asset is suddenly terminated is ordi-

> narily allowed for under the loss provisions of the statute, the loss being deductible in its entirety in the year in which it occurs. * * *

See also *id.*, p. 662, Section 20.114.

Although the same type of circumstance, such as prohibitory legislation or a new invention, may give rise to either deduction, depending on the celerity with which it is effective in terminating useful value, the loss deduction, granted under a different statutory provision, is entirely separate and different from the obsolescence deduction, and a claim for one will not support the other deduction. *Olean Times-Herald Corporation* v. *Commissioner,* 37 B. T. A. 922; *Alliance Milling Co.* v. *Commissioner,* 10 B. T. A. 457; cf. *Best Brewery Co.* v. *Commissioner,* 16 B. T. A. 1354; see *Red Wing Malting Co.* v. *Willcuts,* 15 F. (2d) 626, 634 (C. C. A. 8th), certiorari denied, 273 U. S. 763; *Kaltenbach* v. *United States,* 66 C. Cls. 581, 588. The question of whether the taxpayer is here entitled to a deduction under the loss provision of the statute will be considered in Point III, *infra.*

B. THE LAND TITLE PLANT DID NOT IN FACT BECOME OBSOLETE DURING THE TAXABLE YEAR

In Point I A, *supra,* we sought to establish that the claimed deduction for obsolescence was correctly denied, as a matter of law, by the court below. We now make the further contention that, even if a deduction for obsolescence might under some circumstances be allowable in a case of this character, nevertheless, no deduction is allowable here, for, as stated by the court

below, the Land Title plant did not in fact become obsolete during the taxable year.

The Land Title plant was originally installed by the Land Title and Trust Company, one of the combining companies, as far back as 1886–1887. (R. 24.) The records therein "went all the way back to William Penn, the original grant" (R. 32), and had been kept scrupulously up to date by the expenditure of very large sums (R. 23) for the purpose of making notations in the plant's files of all transactions pertaining to real estate titles in Philadelphia from 1886 until October, 1927 (R. 288). In view of these facts, it is patently absurd for taxpayer to maintain that the plant became obsolete and worthless, except for salvage value, merely because current recordings were discontinued during one year, the taxable period November 1, 1927, to October 31, 1928. As the court below trenchantly stated (R. 325):

> To hold that the plant became obsolete within the taxable year is contrary to the facts. True, it was not as useful at the end of the taxable year as at its beginning, but to conclude that a title plant created between the years 1886 and 1887, steadily added to and kept up to date until October, 1927, loses its usefulness in the following twelve months because of a failure to add current notations to its records is contrary to reason. There is no adequate evidence of record in the case at bar to sustain such a view. * * *

Taxpayer's claim that the Land Title plant, which it carried on its books at $800,000, became worthless, ex-

cept for salvage value, because of obsolescence during the taxable year is seen to be little short of fantastic in view of the fact that taxpayer set a price upon it to a prospective purchaser, several months after the beginning of the taxable year, of $1,000,000. (R. 33–34, 41, 297.) Moreover, its goodwill was said to be "very substantial". (R. 96–97.) It should be noted also that for purposes of the merger the Land Title plant was valued at $800,000, the same amount at which the Real Estate title plant was valued. This amount was $525,000 more than the value at which the Land Title plant had been carried immediately prior to the merger. (R. 22.) In its report to the Commonwealth of Pennsylvania for the two-month period from its organization on November 1, 1927, to December 31, 1927, taxpayer listed among its assets "Title Plant", valued at $1,600,000, which item consisted of the Land Title plant and the Real Estate title plant, each carried on its books at $800,000. (R. 22.) In its reports for the calendar years 1928, 1929, and 1930, the value assigned to the item "Title Plant" was reduced by $50,000 each year. (R. 27.) The high value placed upon the Land Title plant on the taxpayer's books, and the annual reductions thereof, presumably for depreciation, are hardly consistent with its contention that the Land Title plant became totally obsolete and valueless, except for salvage, in the taxable year 1928. In the year in which an asset becomes totally obsolete, its value is not enhanced by $525,000, nor is the value of a totally obsolete asset subject to further depreciation. See *Lattimore* v. *United States*, 12 F. Supp. 895, 910 (C. Cls.).

Further, the Annual Operating Statement of the Land Title and Trust Company for its fiscal year ending September 30, 1927 (R. 262–263) discloses total expenditures on account of the Land Title plant amounting to $167,821.82, of which only $12,142.72 was spent on searches. Other items included rent, $18,650.04, salaries, $114,904.37, and stationery, $22,124.69. Apparently a substantial part of these expenditures must have been incurred in operating the plant, not merely in keeping it up to date, although no precise breakdown is possible on the basis of the data in the operating statement. Even assuming, as could not possibly have been the case, that the entire amount expended during the fiscal year ended September 30, 1927, $167,821.82, was spent for the sole purpose of keeping the plant up to date during that fiscal period, the expenditure necessary to keep the same plant up to date for a similar period, the taxable year November 1, 1927, to October 31, 1928, would scarcely have been greater than $167,821.82. It thus appears that during the taxable year, by an expenditure of such a sum, the plant could have been kept up to date. We submit that an asset of an alleged value of over $1,000,000 could not have become totally obsolete and worthless, except for salvage value, merely because of the failure to spend $167,821.82, or some part thereof, on keeping it up to date during the taxable year. It would seem that, even at the end of the taxable year, by an expenditure of such an amount, taxpayer could have restored the Land Title plant to a perfectly up to date condition. Indeed, it would have cost taxpayer considerably less, since tax-

payer would merely have had to copy the entries from the up to date Real Estate Title plant. (R. 106, 121.)

The conclusion is therefore inescapable that the Land Title plant did not in fact become obsolete during the taxable year. Nevertheless, the District Court determined that the Land Title plant "was the subject of obsolescence during the plaintiff's fiscal year commencing November 1, 1927 and ending October 31, 1928 and became obsolete on or before October 31, 1928." (R. 297.) Taxpayer argues that the District Court's findings are conclusive (Br. 33–38). But whether denominated a finding of fact or conclusion of law, the District court's determination was actually a ruling on a mixed question of law and fact which may be reviewed on appeal. *Helvering* v. *Tex-Penn Co.*, 300 U. S. 481, 491; *Bogardus* v. *Commissioner*, 302 U. S. 34, 39. And it is even further established that where the record contains the evidence and reveals that an ultimate finding of fact is clearly erroneous, unsupported by any evidence, the appellate court is not bound thereby, but may disregard the finding and reverse the judgment. *United States* v. *Clark*, 96 U. S. 37; *First National Bank of Chicago* v. *United States*, 102 F. (2d) 907 (C. C. A. 7th); *Conners* v. *United States*, 141 Fed. 16 (C. C. A. 1st). See *Collier* v. *United States*, 173 U. S. 79, 81; *United States* v. *Buffalo Pitts Co.*, 234 U. S. 228, 232; *United States* v. *Union Trust Co. of Indianapolis*, 90 F. (2d) 702, 703 (C. C. A. 7th).

In the instant case, there is nothing in the entire record to support the ultimate conclusion that the plant "became obsolete on or before October 31, 1928". (R. 297.) Even assuming that such finding involved

purely a question of fact, it is not conclusive. The only evidence of record probative in any way of obsolescence is the testimony that no new entries were made after October, 1927. (R. 50, 422.) But that evidence is assuredly no support for the ultimate finding of total obsolescence on or before October 31, 1928, particularly in the light of all the other evidence as to the completeness of the plant's records, the heavy investment in the plant, the relatively small cost of keeping it up to date for one year, its valuation by taxpayer for purposes of the merger at $800,000 on November 1, 1927, the price of $1,000,000 set upon it in 1928, the continuing high valuation in subsequent years, and the deductions for depreciation in subsequent years' reports to the Commonwealth of Pennsylvania. Accordingly, the finding of the District Court is not conclusive, and the holding of the court below may be upheld on the ground that the Land Title plant did not in fact become obsolete during the taxable year.

II

ASSUMING, ARGUENDO, THAT TAXPAYER IS OTHERWISE ENTITLED TO A DEDUCTION FOR OBSOLESCENCE, THE ALLOWANCE IS PRECLUDED BECAUSE THE PROPERTY WAS NOT "USED" IN THE TRADE OR BUSINESS AS REQUIRED BY SECTION 23 (K) OF THE REVENUE ACT OF 1928

By the express and unambiguous language of Section 23 (k) of the Revenue Act of 1928, the allowance for exhaustion and wear and tear, including obsolescence, is limited to "property *used* in the trade or business" (italics supplied). It is beyond question that unless the property is so used, no deduction for obsolescence in any amount may be had. *Kansas City Southern Ry. Co.*

v. *Commissioner,* 52 F. (2d) 372 (C. C. A. 8th), certiorari denied, 284 U. S. 676; *Buck* v. *Commissioner,* 83 F. (2d) 627 (C. C. A. 9th); *Jewett & Co.* v. *Commissioner,* 61 F. (2d) 471 (C. C. A. 2d); *Des Moines Title Co.* v. *Commissioner,* 39 B. T. A. 729.[6] In *Buckwalter* v. *Commissioner,* 61 F. (2d) 571 (C. C. A. 6th), it was held that no deduction is allowable for the exhaustion of unexploited patents owned by a corporate officer who refrained from prosecuting infringers because they were customers of his employer. Such property, the court held, was not "used in the trade or business", assuming that the taxpayer was engaged in a trade or business, even though the taxpayer's failure to enforce his rights under the patent may have redounded to his financial benefit by placing him in better grace with his employer.

In the opinion below, the Circuit Court of Appeals intimated that it believed the taxpayer had not complied with the statutory condition precedent of use in the trade or business (R. 321–322), but it did not rest its decision on that ground. We now contend that the Circuit Court of Appeals would have been entirely justified in denying the deduction on the ground that the stored plant was never used in the taxpayer's business within the meaning of the statute, for its use had ceased prior to the merger creating the taxpayer corporation.

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[6] There is nothing contrary to the above cases in *Kittredge* v. *Commissioner,* 88 F. (2d) 632 (C. C. A. 2d), which merely held that the deduction may be had for business property, though temporarily idle, if still "devoted to the trade or business" and not withdrawn from business purposes.

The evidence relating to the issue of use of the Land Title plant is summarized by the District Court as follows (R. 288):

> In October and continuing through part of November, 1927, the Land Title plant was removed from the former offices and *stored* at 517 Chestnut Street where it has remained to the present time. It was used at first in connection with title matters then pending, especially those relating to properties *to be sold* at the Sheriff's sale of *November,* 1927, and subsequently only on infrequent occasions as a reference to avoid the necessity of inspecting the public records. The plant was never continued by the addition of current recordings, * * *. [Italics supplied.]

As correctly pointed out by the Circuit Court of Appeals, "There is no evidence * * * to show that the plant was used in connection with new searches of properties after October 31, 1927." (R. 321.) The merger creating the taxpayer corporation did not take place until October 31, 1927, and taxpayer did not open for business until November 1, 1927. (R. 21–22.) The testimony of taxpayer's title officer, as observed by the Circuit Court of Appeals, is highly significant, for it reveals that the Land Title plant was not used during taxpayer's existence. As title officer, he presumably would have more knowledge of the use made of the title plant than any of the other officers. He testified (R. 56–57):

> Q. When were the records put down there?
>
> A. The records were taken down there sometime between the second week in October and the

end, I think, of the first week in November, or perhaps a little later.

Q. Of what year?

A. Of 1927.

Q. And what hapened to them after they were put there? Were they used or not?

A. The only use made of them *in October,* that I know of, was that the block plan books, which were sent down first, were used as a means of ascertaining what insurances were involved in connection with the *forthcomihg Sheriff sales of November,* it having been the custom to look at such insurances to make sure that the Sheriff sales were not upon any liens which affected the title as of the date that we had insurance—to any such properties. *And outside of that I have no personal knowledge of what reference may have been made, from time to time, after the first of November, when the new company went into operation,* what references may have been made from time to time to that plant. (Tr. 66.)

Q. You do know that they looked up some things from time to time?

A. But I believe, from time to time, there has been, very occasionally, a check-up of some information from material in the plant to save a visit to City Hall. [Italics supplied.]

Similarly, taxpayer's president testified that (R. 32):

> The Land Title plant had to be used for a very short time in part on account of the time element with respect to Sheriff's sales of *the coming month, the month of November,* and I think December, although I can't say definitely on that. * * * [Italics supplied.]

It will be noted that both witnesses referred to the month of November as being in the future. Thus it is evident that even the slight use referred to in connection with the sheriff's sales took place in October, 1927, prior to the merger creating the taxpayer, on October 31, 1927, and prior to its opening for business on November 1, 1927. (R. 21–22.) The record is absolutely devoid of any indication that the Land Title plant was used during the taxpayer's existence other than the title officer's mere "belief" that "very occasionally" there was some incidental reference to the records in the Land Title plant in order to avoid the slight inconvenience of a visit to the City Hall.

Moreover, in taxpayer's report to the Pennsylvania Department of Revenue it is stated that (R. 29): "These Title Plants being duplicates, *one of them was of no further use, and was immediately discarded* * * * ." [Italics supplied.] Indeed, while interrogating taxpayer's witness with a view to establishing obsolescence during the taxable year, taxpayer's own counsel unwittingly made the damaging admission that the plant was taken out of use prior to the creation of the taxpayer corporation when he asked this question (R. 77):

> Q. Let me ask you to say what the difference was in the plant *after it had been taken out of use in October, 1927, and stored in the basement*, 517 Chestnut Street—what would the difference be in the plant by October 31, 1928? [Italics supplied.]

The witness' reply seems to indicate that the plant was taken out of use by October 31, 1927. (R. 78).

Thus, the evidence necessitates the conclusion that the property was stored and its use in the business terminated prior to the organization of the taxpayer. In any event, however, there is absolutely no evidence of record any more favorable to the taxpayer than a "belief" that the Land Title plant was "very occasionally" and incidentally referred to, as a "check-up", in order "to save a visit to City Hall". (R. 57.) As stated by the Circuit Court of Appeals "that use at most was very slight". (R. 322.)

Notwithstanding the evidence set out above, and its own findings that daily entries ceased in October, 1927 (R. 296), and that the plant was put in storage in late October and early November, 1927 (R. 296), the District Court, in its findings of fact, included the following (R. 296): "The title plant formerly owned by the Land Title and Trust Company was used in the business of the plaintiff-petitioner after the merger in November 1927". However, no finding is made as to the extent or character of such use. If the finding as to use be considered a reference to the negligible and incidental use of the plant, as a slight convenience, indicated by the foregoing testimony, we do not challenge its validity, but assert that the District Court erred as a matter of law in holding that such negligible use constitutes a sufficient satisfaction of the statutory requirement of "use in the trade or business". If, on the other hand, the finding be interpreted to mean that the plant was used in taxpayer's business in any real or substantial sense, then we assert the finding is a nullity, wholly devoid of support in the record, contrary

to all the facts and inconsistent with the court's own findings that the plant was stored in the basement in the latter part of October and early November, 1927, and that daily entries therein were discontinued in October, 1927.

III

TAXPAYER IS NOT ENTITLED TO ANY DEDUCTION UNDER SECTION 23 (F) OF THE REVENUE ACT OF 1928 ON THE GROUND OF ABANDONMENT OF A CAPITAL ASSET

Taxpayer contends that it is "clearly entitled to a deduction on the theory of abandonment as well as on the theory of obsolescence". (Br. 38–48.) As the taxpayer apparently recognizes (Br. 12), its "abandonment" claim, if allowable at all, must be based on the entirely different statutory provisions in Section 23 (f), granting a deduction for *losses*. Yet it will be shown that taxpayer is not entitled to a loss deduction because of abandonment for the following reasons: (1) the evidence reveals that the asset in question was neither abandoned nor otherwise disposed of, nor did it become worthless, during the taxable year; (2) it was known when the property was acquired that it was a duplicate and would not be useful in taxpayer's business; (3) it was acquired to eliminate competition; (4) taxpayer's claim for refund is inadequate to support such a claim.

(1) Manifestly, to obtain the claimed abandonment deduction, abandonment must be proved. *Terre Haute Electric Co.* v. *Commissioner*, 96 F. (2d) 383 (C. C. A. 7th). This follows from the established requirement that a loss, to be deductible, must be fixed by some

identifiable event, such as a sale or other disposition, or some occurrence indicating a closed transaction. *United States* v. *White Dental Co.*, 274 U. S. 398; *United States* v. *Hardy*, 74 F. (2d) 841 (C. C. A. 4th). While abandonment necessarily involves non-use, mere non-use obviously does not constitute abandonment. *Ewald Iron Co.* v. *Commissioner*, 37 B. T. A. 798; *Zumwalt* v. *Commissioner*, 25 B. T. A. 566. Neither does the fact that, in addition to non-use, the asset in question was dismantled or stored, or both. *Ewald Iron Co.* v. *Commissioner, supra*; *Flexible File Co.* v. *Commissioner*, 13 B. T. A. 909, affirmed, *per curiam*, 41 F. (2d) 597 (C. C. A. 6th).

Whether there has been an abandonment has been said to depend on the intention of the taxpayer, coupled with an act of abandonment, both to be determined from the surrounding facts and circumstances. *Belridge Oil Co.* v. *Commissioner*, 11 B. T. A. 127; *Reuben H. Donnelley Corporation* v. *Commissioner*, 26 B. T. A. 107; *Zumwalt* v. *Commissioner, supra*; *Ewald Iron Co.* v. *Commissioner, supra*.

Applying the foregoing principles to the case at bar, it is apparent that taxpayer has failed to show abandonment of the Land Title plant. Taxpayer stored, but did not scrap the plant. The place of storage was a dry, heated, illuminated basement, where the plant was not subject to any physical deterioration (R. 107, 108), and the records stored there were kept fully intact and available for use (R. 59, 69). Taxpayer's president testified that in the Spring of 1928, after it had been in storage for approximately half the taxable

year, he quoted a price on it to a prospective purchaser of $1,000,000. (R. 33.) He further testified that the possession of such a plant was a distinct advantage to any company in the title insurance business because a company owning such a plant would be "better prepared to command the business than otherwise * * *." (R. 36.) The taxpayer's title officer characterized the Land Title plant as "complete" and "admirable" (R. 50), with records going back further than any other plant in the city, including the Real Estate plant (R. 60–61), and taxpayer's president testified that it was "a more complete plant than any other plant in the City; it had a background which went all the way back to William Penn, the original grant" (R. 32). Moreover, even the District Court found that the Land Title plant had a value of $125,000 at the end of the taxable year. (R. 298.) On these facts, it is no less than preposterous for taxpayer to claim that it abandoned the plant. The most that can be said is that taxpayer stored the plant because it was surplus equipment, and for that reason ceased making the daily entries necessary to keep it up to date. As pointed out by the Circuit Court of Appeals (R. 323), at any time during the taxable year, at an expense not incommensurate with the value placed upon it, taxpayer could have restored the Land Title plant to perfect operating condition.[7]

[7] In this connection it may be noted that taxpayer's title officer and an expert witness for the Government each testified that the cost of bringing one plant up to date is much less where its owner has another plant which has been kept up to date, from which the entries can be copied, than would otherwise be the case. (R. 106, 121.) See *supra*, pp. 25–26, for discussion of necessary expenditure.

Clearly, the Land Title plant was not discarded and it had substantial value at the end of the taxable year. Under these circumstances, it is submitted that taxpayer has failed to establish abandonment, the ground on which the loss deduction must be claimed. Since the taxpayer has failed to sustain its burden of proof the deduction should be disallowed. *Burnet* v. *Houston,* 283 U. S. 223; *United States* v. *Anderson,* 269 U. S. 422.

(2) Furthermore, taxpayer is not entitled to the deduction because, at the time of acquisition, taxpayer knew that the Land Title plant would not be useful in its business since it was a duplicate of taxpayer's other plant. (R. 35.) This was admitted in taxpayer's report to the Pennsylvania Department of Revenue (R. 43), and may be inferred from testimony of the expert witness for the United States to the effect that where one company acquires two complete title abstract plants it will certainly be feasible to use only one of them (R. 170–171, 177). The fact that it was the Land Title plant, not the Real Estate Title plant which it was intended at the time of acquisition not to use is indicated by testimony of taxpayer's title officer that, at the time of the merger in October, 1927, he and taxpayer's vice president, who were jointly entrusted with the task of determining which plant should be used, "had been convinced for some time that the Land Title plant * * * was a very expensive and uneconomical plant to keep up and maintain". (R. 50.) Moreover, the same officer testified that the decision to use the Real Estate Title plant and store the Land

Title plant was reached "after perhaps an hour and a half or two hours' visit to the plant". (R. 50.) The foregoing circumstances, considered in conjunction with the fact that the Land Title plant was stored in October and early November, 1927 (R. 57, 296), renders inescapable the conclusion that at the time the Land Title plant was acquired it was not intended to be used.

The principle is firmly established that no loss deduction on grounds of abandonment of a capital asset is permissible where, at the time the property was acquired, there was no intention to use it. Thus, "when a taxpayer buys real estate upon which is located a building, which he proceeds to raze with a view to erecting thereon another building, it will be considered that the taxpayer has sustained no deductible loss by reason of the demolition of the old building". Regulations 74, Article 172;[8] *Providence Journal Co.* v. *Broderick*, 104 F. (2d) 614 (C. C. A. 1st); *Liberty Baking Co.* v. *Heiner*, 37 F. (2d) 703 (C. C. A. 3d); cf. *Anahma Realty Corp.* v. *Commissioner*, 42 F. (2d) 128 (C. C. A. 2d), certiorari denied, 282 U. S. 854; *Young* v. *Commissioner*, 59 F. (2d) 691 (C. C. A. 9th), certiorari denied, 287 U. S. 652; *Spinks Realty Co.* v. *Burnet*, 62 F. (2d) 860 (App. D. C.), certiorari denied, 290 U. S. 636. See also *Union Bed & Spring Co.* v. *Commissioner*, 39 F. (2d) 383, 385 (C. C. A. 7th). The intention of the taxpayer as to use at the time of purchase is the test of

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[8] The identical provision appears in Article 142 of Regulations 45, 62, 65 and 69, and has been retained in regulations pursuant to subsequent revenue acts in Article 172 of Regulations 77, and Article 23 (e) 2 of Regulations 86, 94 and 101.

whether the loss deduction is allowable. *Providence Journal Co.* v. *Broderick, supra; Union Bed & Spring Co.* v. *Commissioner, supra;* cf. *Hotel McAllister* v. *United States,* 3 F. Supp. 533 (S. D. Fla.). Applying the principle underlying the foregoing authorities to the instant case, taxpayer's intention not to use the Land Title plant bars any claim for a loss deduction on ground of abandonment.

(3) Where a taxpayer acquires property in order to eliminate competition, the transaction does not give rise, on disposition of the property thus acquired, to a deductible loss, for the value of the thing procured, the elimination of competition, is a capital asset. *Newspaper Printing Co.* v. *Commissioner,* 56 F. (2d) 125 (C. C. A. 3d).[9] See also *Putnam Trust Co.* v. *Commissioner,* 26 B. T. A. 655. Similarly, it has repeatedly been held that expenses for the purpose of eliminating

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[9] In *Sanitary Co. of America* v. *Commissioner,* 34 F. (2d) 439 (C. C. A. 3d), cited by taxpayer (Br. 13), a loss deduction was allowed when taxpayer purchased and scrapped the plant of a competitor. However, the only question argued or considered by the court was whether the taxpayer's mode of ascertaining its loss was proper. No objection appears to have been made to the claimed deduction on the ground that the purpose of the purchase was the elimination of competition, either before the Court of Appeals or in the Board of Tax Appeals, where the deduction was disallowed solely on the ground of insufficient evidence as to cost. 10 B. T. A. 944. Accordingly, the case is hardly authority for the proposition that a deductible loss is sustained where a plant is purchased and scrapped for the purpose of eliminating competition. Apparently the very court which decided it did not consider it to be such, for it is not even mentioned in that court's subsequent opinions in the *Newspaper Printing* and *Clark Thread* cases, *supra;* or in the instant case, in which the court cites with approval the *Newspaper Printing* case (R. 326).

competition constitute capital expenditures, and are not deductible as ordinary and necessary business expense, since a capital asset is acquired. *Clark Thread Co.* v. *Commissioner,* 100 F. (2d) 257 (C. C. A. 3d); *Houston Natural Gas Corp.* v. *Commissioner,* 90 F. (2d) 814 (C. C. A. 4th); *Public Opinion Pub. Co.* v. *Jensen,* 76 F. (2d) 494 (C. C. A. 8th); *Eagle Pass & Piedras Negras Bridge Co.* v. *Commissioner,* 23 B. T. A. 1338; *News Leader Co.* v. *Commissioner,* 18 B. T. A. 1212; *Record Abstract Co.* v. *Commissioner,* 2 B. T. A. 628.[10]

Although the Circuit Court of Appeals in the present case held that taxpayer could not claim the deduction on the ground of abandonment because it did not assert such ground in its refund claim, the court went on to say that "the circumstances of the case at bar seem to us to be closely analogous to those presented in *Newspaper Printing Co.* v. *Commissioner,* 56 F. (2d) 125, decided by this court". (R. 326.) In that case the court denied a loss deduction upon the disposition of certain assets because it affirmatively appeared that the purpose of the purchase of such assets was the elimina-

[10] The *Record Abstract* case, it may be noted, involved a situation in which an abstract company obtained the abstract books of a competitor, for the purpose of eliminating competition. The cost of the acquisition was held a capital expenditure. Indeed, in the very case upon which taxpayer places principal reliance, *Crooks* v. *Kansas City Title & Trust Co.*, 46 F. (2d) 928, 929 (C. C. A. 8th), the court declared that taxpayer would not be entitled to any deduction for obsolescence on the four abstract plants in question if it appeared that its motive in acquiring these plants was the elimination of competition, but the court pointed out that the trial court had there held that such was not the case.

tion of competition. In other words, therefore, the Circuit Court of Appeals in the present case was of the opinion that the motivating force in the merger which resulted in the formation of the taxpayer corporation and its acquisition of two duplicate abstract plants was the desire to eliminate competition.

In the light of the evidence, such purpose, or something very closely analogous to it, must be imputed to taxpayer. As a result of the merger, taxpayer acquired the two most complete of the three principal abstract plants in Philadelphia (R. 35, 80), although only one of them could economically be used (R. 29, 118–119, 124). The parties to merger knew, at and before the time of the merger, that both plants were "designed and used for the same general purpose". (R. 22–23.) Ownership of a complete abstract plant is an invaluable aid in "commanding the business" of title insurance, according to the testimony of taxpayer's president (R. 36), and is a source of great prestige in the business (R. 119). Certain important customers, such as large mortgage and insurance companies, would not give their title insurance business to a company which did not own an abstract plant. (R. 36, 119.) Finally, attention is respectfully invited to the wholly uncontroverted and unimpeached testimony of the expert witness for the United States to the effect that it would be highly advantageous "to shut out competition among the so-called plant companies" and that "the suppression of one of the existing plants in the City would be a financial benefit to the other companies owning plants at that time". (R. 119–120.) Accordingly,

no deduction, whether for obsolescence or for abandonment, is permissible.

(4) Moreover, there is considerable doubt as to whether the "abandonment" issue may even be raised. The Circuit Court of Appeals held that the taxpayer could not claim a loss deduction on grounds of abandonment, stating that the claim for refund was based "solely upon the ground of obsolescence". (R. 326.) The accuracy of that statement is fully substantiated by the refund claim itself. (R. 8–12.) Taxpayer does not deny that its refund claim was based solely on obsolescence. Indeed, in its petition, taxpayer avers that it filed its claim for refund "alleging as the basis of its claim that it was entitled to a loss due to obsolescence of the title insurance plant * * *". (R. 6.) The refund claim was never amended.

Where a suit to recover taxes erroneously paid is based upon the rejection of a refund or credit claimed, it must rest upon the ground stated in the claim as originally filed, or as properly amended. It has repeatedly been held that recovery upon some ground other than that specified in the refund claim is not permissible. *United States* v. *Felt & Tarrant Mfg. Co.*, 283 U. S. 269; *Lucky Tiger-Combination Gold Mining Co.* v. *Crooks*, 95 F. (2d) 885 (C. C. A. 8th); *Continental-Illinois Nat. Bank & Trust Co.* v. *United States*, 67 F. (2d) 153 (C. C. A. 7th), certiorari denied, 291 U. S. 663; *Ferguson* v. *United States*, 2 F. Supp. 1012 (C. Cls.), certiorari denied, 290 U. S. 694; cf. *Duffin* v. *Lucas*, 55 F. (2d) 786 (C. C. A. 6th), certiorari denied, 287 U. S. 611. And in *Red Wing Malting Co.* v. *Willcuts*, 15 F. (2d)

626, 634 (C. C. A. 8th), certiorari denied, 273 U. S. 763, and *Kaltenbach* v. *United States,* 66 C. Cls. 581, 588, it was held that where the claim for refund is based on obsolescence, taxpayer may not urge that it is entitled to a deduction under the loss provision of the statute.[11]

Under the foregoing decisions, a taxpayer may not recover on the basis of a loss deduction when, as is here concededly the case, in its claim for refund it sought only a deduction on grounds of obsolescence. Taxpayer, however, argues that the question of abandonment was submitted to the Commissioner, although not presented in the refund claim. (Br. 40.) This argument is based on the fact that the letter from the Deputy Commissioner advising that the claim would be rejected states "Your claim is based on the statement that the title plant formerly owned by the Land Title and Trust Company became obsolete and was abandoned". (R. 13.) Taxpayer emphasizes the use of the word "abandoned" and urges that this letter proves that the question of abandonment was submitted to the Commissioner. Two answers may be made to this contention. First, on the question of what was submitted to the Commissioner, resort must manifestly be had to the document submitting the claim, the refund claim itself, which, taxpayer does not deny, was based

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[11] The analogous question of whether a claim for refund may be amended, after expiration of the period of limitation, so as to claim the refund on another ground, was recently considered by this Court in *United States* v. *Andrews*, 302 U. S. 517, and *United States* v. *Garbutt Oil Co.*, 302 U. S. 528. These cases establish the rule that such amendment of a previously filed refund claim may not be made when the amendments state a ground different from that stated in the original claim.

solely on obsolescence. Second, even though the Deputy Commissioner's letter may indicate what was actually considered by the Bureau, it does not support taxpayer's position that the Bureau considered two grounds of deduction, obsolescence and abandonment. For, when the passage relied upon is read in its context (R. 13), it indicates that the Bureau considered the matter as involving only one question, that of obsolescence, and that it regarded the abandonment as merely implementing that claim, not as giving rise to a separate question under a different statutory provision.[12] Indeed, petitioner fails to quote the entire sentence upon which it relies (Br. 40), and which, in full, reads as follows (R. 13):

> Your claim is based on the statement that the title plant formerly owned by the Land Title and Trust Company became obsolete and was abandoned; that the plant had a value of $1,250,000.00, and, therefore, a loss *on account of obsolescence* should be allowed in this amount. [Italics supplied.]

[12] The petition (R. 2–8) presented the case to the District Court on the sole ground that taxpayer was entitled to a deduction for obsolescence under Section 23 (k) of the Revenue Act of 1928, and the trial court's statement of the question presented to it appears to be limited to a deduction for obsolescence (R. 289). Accordingly, the new issue of a loss deduction under Section 23 (k) on the ground of abandonment of a capital asset could not be raised on appeal. *General Utilities Co.* v. *Helvering*, 296 U. S. 200; *Helvering* v. *Salvage*, 297 U. S. 106. Cf. *Tricou* v. *Helvering*, 68 F. (2d) 280 (C. C. A. 9th), certiorari denied, 292 U. S. 655, rehearing denied, 293 U. S. 629; *Botchford* v. *Commissioner*, 81 F. (2d) 914 (C. C. A. 9th). See also *Duignan* v. *United States*, 274 U. S. 195; *Kottemann* v. *Commissioner*, 81 F. (2d) 621 (C. C. A. 9th).

IV

EVEN IF TAXPAYER IS ENTITLED TO SOME DEDUCTION, THE AMOUNT ALLOWED BY THE DISTRICT COURT IS EXCESSIVE

1. The complete Land Title plant consisted of two distinct parts: (1) the title search plant, consisting of the full set of records relating to real estate titles, and (2) the separate applications, abstracts, and opinions in each matter for which the company issued its title insurance policy. (R. 40, 49, 61.) As only the first part of the search plant allegedly became obsolete and was allegedly abandoned, it is clear that the March 1, 1913 value of the entire plant must be apportioned as between its two constituent parts, and only the value appertaining to the search plant, less its salvage value, may be deducted. It is not clear that the petitioner's witnesses or the District Court itself excluded the value of (2) in arriving at the March 1, 1913 value (R. 79, 83, 93, 100–103, 297–298).

2. Moreover, the District Court erred in finding the March 1, 1913 value to be $1,000,000. (R. 297.) It is stipulated that immediately prior to the merger in 1927 the Land Title plant was carried on the books of the Land Title and Trust Company, its then owner, at only $275,000 (R. 22), at which figure it was valued from September 30, 1897 (R. 23). Also, on its federal capital stock tax returns for the years 1917 to 1926, inclusive, the Land Title and Trust Company returned the book value and fair value of the Land Title plant at $275,000. (R. 24.) Even for purposes of the merger,

the Land Title plant was valued at only $800,000. (R. 22.) It was originally acquired, during the years 1886 and 1887 at a cost of $251,509.84. Expenses on additions to and maintenance of the plant during the years 1888, 1889 and 1890 amounted to $24,541.78, and from 1890 to February 28, 1913, the sum of $317,645.36 was spent on the plant. (R. 23.) These facts do not justify a finding that the March 1, 1913 value was $1,000,000. The only evidence in the record in any way probative of a March 1, 1913 value of $1,000,000 is the opinion evidence given by interested witnesses (R. 75, 83, 102), without adequate supporting facts. Such evidence is not conclusive. See *Dayton P. & L. Co.* v. *Comm'n,* 292 U. S. 290, 299–300, and authority there cited. It may be disregarded in favor of admitted facts. *Balaban & Katz Corp.* v. *Commissioner,* 30 F. (2d) 807, 808 (C. C. A. 7th); *State Line & Sullivan R. Co.* v. *Phillips,* 98 F. (2d) 651 (C. C. A. 3d), certiorari denied, 305 U. S. 635. Since the finding of a March 1, 1913 value of $1,000,000 is based solely upon opinion evidence of interested witnesses, and is inconsistent with the stipulated facts set out *supra,* all of which indicate a much lower value, we submit that the District Court's finding is erroneous and should be disregarded.

3. The District Court also erred in another respect. Testimony as to the value of the Land Title plant included the element of good will, which was said to be "very valuable" and "very substantial", although the witness was unable to estimate its value more precisely.

(R. 83–85, 97.) But no deduction may be taken for the obsolescence of good will. See *Clarke* v. *Haberle Brewing Co.*, 280 U. S. 384, as explained in *Gambrinus Brewery Co.* v. *Anderson*, 282 U. S. 638, 641–642. See also *Red Wing Malting Co.* v. *Willcuts*, 15 F. (2d) 626 (C. C. A. 8th), certiorari denied, 273 U. S. 763; *Kaltenbach* v. *United States*, 66 C. Cls. 581; *Moise* v. *Burnet*, 52 F. (2d) 1071 (C. C. A. 9th). In accordance with these decisions, Treasury Regulations 74, Article 203, expressly provide that "No deduction for depreciation, including obsolescence, is allowable in respect of good will." Hence, the District Court erred in not excluding from the value of the Land Title plant such part thereof as was attributable to its "very substantial" good will.[13]

Finally, it would seem that good will is something which attaches to a business rather than to any specific physical property. Thus, as a result of the merger, taxpayer acquired the good will attributable to the title search and insurance business of the Land Title and Trust Company. Such good will, we submit, was retained by taxpayer despite the alleged obsolescence and abandonment of the physical title plant, because tax-

[13] The District Court apparently conceded that the value of the good will should not be included in determining the value of the plant as of March 1, 1913 (R. 144), but overlooked the fact that the two witnesses who testified that the plant had a value of $1,250,000 and $1,000,000 respectively had both relied on the value of the good will in making their valuations of the plant and that there was no evidence establishing the value of the good will separately. (R. 75, 83, 90–91, 102–103.) In making its finding that the plant had value of $1,000,000 the court merely accepted the lower of these estimates.

payer continued to engage in the title search and insurance business. Accordingly, the deduction on account of the Land Title plant should be limited to its value on March 1, 1913, exclusive of any good will value attaching to the business in which it was then employed.

CONCLUSION

The decision of the court below is correct and should be affirmed. However, if it be held that taxpayer is entitled to some deduction, the case should be remanded to the District Court for correct determination of the amount allowable.

Respectfully submitted.

ROBERT H. JACKSON,
Solicitor General.

SAMUEL O. CLARK, Jr.,
Assistant Attorney General.

SEWALL KEY,
HELEN R. CARLOSS,
ARNOLD RAUM,
HOWARD D. PACK,
Special Assistants to the Attorney General.

DECEMBER, 1939.

APPENDIX

Revenue Act of 1928, c. 852, 45 Stat. 791:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(f) *Losses by corporations.*—In the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise.

* * * * *

(k) *Depreciation.*—A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence. * * *

Treasury Regulations 74 (1929 ed.):

ART. 173. *Loss of useful value.*—When, through some change in business conditions, the usefulness in the business of some or all of the capital assets is suddenly terminated, so that the taxpayer discontinues the business or discards such assets permanently from use in such business, he may claim as a loss for the year in which he takes such action the difference between the basis (adjusted as provided in section 111 and article 561) and the salvage value of the property. This exception to the rule requiring a sale or other disposition of property in order to establish a loss requires proof of some unforeseen cause by reason of which the property has been prematurely discarded, as, for example, where an increase in the cost or change in the manufacture of any product makes it necessary to abandon such manufacture, to which special

machinery is exclusively devoted, or where new legislation directly or indirectly makes the continued profitable use of the property impossible. This exception does not extend to a case where the useful life of property terminates solely as a result of those gradual processes for which depreciation allowances are authorized. It does not apply to inventories or to other than capital assets. The exception applies to buildings only when they are permanently abandoned or permanently devoted to a radically different use, and to machinery only when its use as such is permanently abandoned. Any loss to be deductible under this exception must be fully explained in the return of income.

ART. 201. *Depreciation.*—A reasonable allowance for the exhaustion, wear and tear, and obsolescence of property used in the trade or business may be deducted from gross income. For convenience such an allowance will usually be referred to as depreciation, excluding from the term and idea of a mere reduction in market value not resulting from exhaustion, wear and tear, or obsolescence. The proper allowance for such depreciation of any property used in the trade or business is that amount which should be set aside for the taxable year in accordance with a reasonably consistent plan (not necessarily at a uniform rate), whereby the aggregate of the amounts so set aside, plus the salvage value, will, at the end of the useful life of the property in business, equal the basis of the property determined in accordance with section 113 and articles 591–604. Due regard must also be given to expenditures for current upkeep. In the case of property held by one person for life with remainder to another person, the deduction for depreciation shall be computed as if the life tenant were the absolute owner of the property so that he will be entitled to the deduction during his life, and thereafter the deduction, if any, will be

allowed to the remainderman. In the case of property held in trust, the allowable deduction is to be apportioned between the income beneficiaries and the trustee in accordance with the pertinent provisions of the will, deed, or other instrument creating the trust, or, in the absence of such provisions, on the basis of the trust income which is allocable to the trustee and the beneficiaries, respectively. For example, if the trust instrument provides that the income of the trust computed without regard to depreciation shall be distributed to a named beneficiary, such beneficiary will be entitled to the depreciation allowance to the exclusion of the trustee, while if the instrument provides that the trustee in determining the distributable income shall first make due allowance for keeping the trust corpus intact by retaining a reasonable amount of the current income for that purpose, the allowable deduction will be granted in full to the trustee.

ART. 202. *Depreciable property.*—The necessity for a depreciation allowance arises from the fact that certain property used in the business gradually approaches a point where its usefulness is exhausted. The allowance should be confined to property of this nature. In the case of tangible property, it applies to that which is subject to wear and tear, to decay or decline from natural causes, to exhaustion, and to obsolescence due to the normal progress of the art, as where machinery or other property must be replaced by a new invention, or due to the inadequacy of the property to the growing needs of the business. It does not apply to inventories or to stock in trade, nor to land apart from the improvements or physical development added to it. It does not apply to bodies of minerals which through the process of removal suffer depletion, other provisions for this being made in the Act. (See sections 23 (1) and 114 and articles 221–257 and 611.) Property kept in repair may, never-

theless, be the subject of a depreciation allowance. (See article 124.) The deduction of an allowance for depreciation is limited to property used in the taxpayer's trade or business. No such allowance may be made in respect of automobiles or other vehicles used solely for pleasure, a building used by the taxpayer solely as his residence, nor in respect of furniture or furnishings therein, personal effects, or clothing; but properties and costumes used exclusively in a business, such as a theatrical business, may be the subject of a depreciation allowance

ART. 206. *Obsolescence.*—With respect to physical property the whole or any portion of which is clearly shown by the taxpayer as being affected by economic conditions that will result in its being abandoned at a future date prior to the end of its normal useful life, so that depreciation deductions alone are insufficient to return the cost (or other basis) at the end of its economic term of usefulness, a reasonable deduction for obsolescence, in addition to depreciation, may be allowed in accordance with the facts obtaining with respect to each item of property concerning which a claim for obsolescence is made. No deduction for obsolescence will be permitted merely because, in the opinion of a taxpayer, the property may become obsolete at some later date. This allowance will be confined to such portion of the property on which obsolescence is definitely shown to be sustained and cannot be held applicable to an entire property unless all portions thereof are affected by the conditions to which obsolescence is found to be due.

U. S. GOVERNMENT PRINTING OFFICE: 1920

SUPREME COURT OF THE UNITED STATES.

No. 229.—OCTOBER TERM, 1939.

The Real Estate-Land Title and Trust Company, Petitioner, *vs.* The United States of America.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

[January 15, 1940.]

MR. JUSTICE DOUGLAS delivered the opinion of the Court.

Petitioner, a Pennsylvania corporation, was formed in October 1927 as a result of a statutory consolidation or merger of three companies. Two of the constituent companies owned title search plants which were among the assets acquired by petitioner as a result of the consolidation. While it was known that two title plants would be acquired on the consolidation, there was at that time no definite plan for their disposition. But an immediate investigation was made and it was decided to store one of the plants in order to effect economies of operation. That was done substantially simultaneously with the consummation of the consolidation. About two months thereafter it was decided that the plant retained in use was adequate and that the one in storage would not be needed. Although for a brief period some slight use appears to have been made of the stored plant,[1] it was not kept up to date by the addition of current recordings. As a result it had only a salvage value by October 31, 1928. Meanwhile, negotiations for its sale had been unsuccessful.

In this action petitioner seeks a refund of income taxes for the fiscal year ended October 31, 1928, based on the refusal of the Collector of Internal Revenue to allow a deduction for obsolescence of this plant. It had been carried on the books of the constituent company at $275,000 and was brought into the consolidation at $800,000. The District Court, however, found that its value on

[1] Evidence of use subsequent to the consolidation or merger is quite tenuous, the only specific instances occurring immediately prior to the actual consummation of the consolidation on October 31, 1927.

March 1, 1913, was $1,000,000; on October 31, 1928, $125,000—making an actual loss of $875,000, which that court allowed as a deduction for obsolescence for the taxable year 1928. It accordingly allowed a refund. That judgment was reversed by the Circuit Court of Appeals (102 F. (2d) 582). We granted certiorari because of the asserted conflict of that decision with *Crooks* v. *Kansas City Title and Trust Co.*, 46 F. (2d) 928.

Sec. 23(k) of the Revenue Act of 1928 (45 Stat. 791) allows as a deduction from gross income a "reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence." Admittedly, if the deduction is allowed under this provision it must be for obsolescence, as there has been no exhaustion, wear or tear of the title plant within the meaning of the Act. Now it is true that in the popular sense a thing which is obsolete is one which is no longer used, a meaning which gives color to petitioner's claim for deduction since there is no question that the title plant here involved is no longer utilized to any degree whatsoever. But the term "allowance for obsolescence", as used in the Act and in the Treasury Regulations, has a narrower or more technical meaning than that derived from the common, dictionary definition of obsolete. The Treasury Regulations[2] state the circumstances under which an allowance for obsolescence of physical property may be allowed, viz., where such property is "being effected by economic conditions that will result in its being abandoned at a future date prior to the end of its normal useful life, so that depreciation deductions alone are insufficient to return the cost (or other basis) at the end of its eco-

[2] Treasury Regulations 74, Art. 206, promulgated under the Revenue Act of 1928, provides in full:

"With respect to physical property the whole or any portion of which is clearly shown by the taxpayer as being affected by economic conditions that will result in its being abandoned at a future date prior to the end of its normal useful life, so that depreciation deductions alone are insufficient to return the cost (or other basis) at the end of its economic term of usefulness, a reasonable deduction for obsolescence, in addition to depreciation, may be allowed in accordance with the facts obtaining with respect to each item of property concerning which a claim for obsolescence is made. No deduction for obsolescence will be permitted merely because, in the opinion of a taxpayer, the property may become obsolete at some later date. This allowance will be confined to such portion of the property on which obsolescence is definitely shown to be sustained and can not be held applicable to an entire property unless all portions thereof are affected by the conditions to which obsolescence is found to be due." See also Bureau of Internal Revenue Bulletin "F", January, 1931.

nomic term of usefulness." This Court, without undertaking a comprehensive definition, has held that obsolescence for purposes of the revenue acts "may arise from changes in the art, shifting of business centers, loss of trade, inadequacy, supersession, prohibitory laws and other things which, apart from physical deterioration, operate to cause plant elements or the plant as a whole to suffer diminution in value." *United States Cartridge Co.* v. *United States,* 284 U. S. 511, 516. See also *Burnet* v. *Niagara Falls Brewing Co.,* 282 U. S. 648, 654. Such specific examples illustrate the type of "economic conditions" whose effect on physical property is recognized as obsolescence by the Treasury Regulations. Others could be mentioned which similarly cause or contribute to the relentless march of physical property to the junk pile. But in general, obsolescence under the Act connotes functional depreciation, as it does in accounting and engineering terminology.[3] More than non-use or disuse is necessary to establish it.[4] To be sure, reasons of economy may cause a management to discard a title plant either where it has become outmoded by improved devices or where it is acquired as a duplicate and therefore is useless. But not every decision of management to abandon facilities or to discontinue their use gives rise to a claim for obsolescence. For obsolescence under the Act requires that the operative cause of the present or growing uselessness arise from external forces which make it desirable or imperative that the property be replaced. What those operative causes may be will be dependent on a wide variety of factual situations. "New and modern methods" appear to have been one of the real causes of abandonment of the title plant in *Crooks* v. *Kansas City Title & Trust Co., supra.* Suffice it here to say that no such external causes are present, for the record shows little more than the desire of a management to eliminate one plant which was a needless duplication of another but which functionally was adequate.[5] The fact that fewer employees were required to operate

[3] Kester, Advanced Accounting (3rd ed. 1933) ch. 10; Hatfield, Accounting (1927) ch. V; Saliers, Depreciation Principles and Applications (3rd ed. 1939) ch. 4; Kester, Depreciation (1924); Transactions, Amer. Soc. C. E., vol. 81, p. 1527 (1917); Marston & Agg, Engineering Valuation (1936) pp. 83-85.

[4] 2 Paul & Mertens, Law of Federal Income Taxation, § 20.114.

[5] According to petitioner's own witnesses, the discarded plant was a "more complete plant than any other plant in the City"; and it had a "background which went all the way back to William Penn".

the one retained than the one discarded is inconclusive here. For this is not the case of acquisition of a new plant to take the place of one outmoded or less efficient. Rather the conclusion is irresistible that the plant was discarded only as a proximate result of petitioner's voluntary action in acquiring excess capacity.

In view of this conclusion, we do not reach respondent's further objections to allowance of this claim on grounds of obsolescence.

But petitioner contends that in any event it has abandoned the plant and hence is entitled to a deduction under § 23(f) of the 1928 Act which allows a corporation to deduct "losses sustained during the taxable year and not compensated for by insurance or otherwise." Whether petitioner has satisfied those requirements we do not decide, for its claim for refund was based exclusively and solely on the ground that it was entitled to an allowance for obsolescence. Hence, in absence of a waiver by the government, *Tucker* v. *Alexander*, 275 U. S. 228, or a proper amendment, petitioner is precluded in this suit from resting its claim on another ground. *United States* v. *Felt & Tarrant Mfg. Co.*, 283 U. S. 269. There has been no amendment and there are no facts establishing a waiver.

Accordingly, the judgment of the Circuit Court of Appeals is

Affirmed.

Mr. Justice ROBERTS and Mr. Justice REED took no part in the consideration or decision of this case.

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